



Section 3.4

Activity 3.4.1

1. Stakeholders that might be interested in Leroy's accounts include:
 - Banks and other creditors
 - Employees
 - Suppliers.
2. Leroy's accounts might have been useful to the following stakeholders because:
 - Banks and other creditors – repayment, risk of default, interest, need for new finance
 - Employees – job security, wages, funds to improve working conditions
 - Suppliers – repayment, risk of default, continued business.
3. a. Accounts can be prepared ethically by:
 - Employing an auditor with an ethical reputation
 - Ethical practices by management.b. FlyNow's accounts might have the following ethical issues:
 - Sale of assets to boost cash flow and profits
 - Cash from recent loan
 - Over-valuation of airplanes
 - Quality of work done on the airplanes increasing their value
 - Delayed payments to creditors.

Activity 3.4.2

1. a. Cosy Corner Retailers profit statement:

		\$
Sales	1500 x \$5	7500
Cost of goods sold	1500 x \$2	3000
Gross profit		4500

- b. Profit might be important for a business because it:

- Is a reward to the owners/shareholders
- Increases the value of the business if it is retained
- Shows how successful the business is.



2. Cambridge Boxes profit statement 2014:

		\$
Sales	$3500 \times \$4$	14000
Cost of goods sold	$3500 \times \$2$	7000
Gross profit		7000

Activity 3.4.3

1. Rodrigues Traders profit and loss account missing values:

- $V = 8000$
- $W = 5000$
- $X = 4000$
- $Y = 3200$
- $Z = 2000$

2. Three stakeholders that would be interested in the profit figures are:

- Banks and other creditors
- Employees
- Shareholders.

3. The reasons these stakeholders might be interested in these accounts could be:

- Banks and other creditors – repayment, risk of default, interest
- Employees – job security, wages, funds to improve working conditions
- Shareholders – profit and dividends, continued business.



Activity 3.4.4

1. Karachi Traders profit and loss account 1:

	\$
Revenue (5000 units @ \$4.00)	20 000
Cost of goods sold (5000@ \$1.60 per unit)	8000
Gross profit	12 000
Overhead expenses	5000
Operating profit (profit before tax and interest)	7000
Finance costs (interest)	1000
Profit before tax	6000
Corporation tax @ 25%	1500
Profit for the year	4500
Dividends paid	1200
Retained profit	3300



2. Karachi Traders profit and loss account 2:

	\$
Revenue (6000 units @ \$3.00)	18 000
Cost of goods sold (6000@ \$0.90) per unit)	5400
Gross profit	12600
Overhead expenses	4500
Operating profit (profit before tax and interest)	8100
Finance costs (interest)	2000
Profit before tax	6100
Corporation tax @ 20%	1220
Profit for the year	4880
Dividends paid	1200
Retained profit	3680

Activity 3.4.5

These items appear in these sections of the balance sheet:

- Company's car – fixed asset
- Work in progress – current assets
- Four-year bank loan – long term liability
- Money owed to suppliers – current liabilities
- Issued share capital – shareholders' funds
- Dividends owed to shareholders – current liabilities
- Value of patents – fixed assets
- Payments due from customers – current liabilities
- Retained earnings – shareholders' funds
- Cash in bank – current assets.



Activity 3.4.6

1. The following balance sheet terms can be defined as:
 - Trade receivables – the value of payments to be received from customers who have bought goods on credit
 - Inventories – stocks held by the business in the form of materials, work in progress and finished goods
 - Current assets – assets that are likely to be turned into cash before the next balance sheet date
 - Shareholders' equity – the value of shares issued to shareholders plus accumulated retained profit.
2. Mauritius Telecom's balance sheet in 2012 and 2013 tells us its position has changed in the following ways. The value of:
 - Fixed assets has fallen
 - Stock has fallen
 - Debtors has increased
 - Cash has increased
 - Total asset has increased
 - Long-term liabilities has increased
 - Current liabilities has fallen
 - Shareholders' equity has increased.
3. a. Accounting information might be useful to a potential investor because it provides information about:
 - Potential profits
 - Cash flow and debt
 - Value of the business and parts of the business.b. Accounting information might be useful to creditors because it provides information about:
 - Potential repayment
 - Cash flow and debt
 - Value of assets for securing loans.

Activity 3.4.7

1. 'Depreciation' is the decline in the estimated value of a fixed asset over time. Assets are items of monetary value that are owned by a business.
2. Straight-line depreciation of the new lathe is: $(\$3\,000\,000 - \$200,000) / 10 = \$280\,000$.
3. Declining balance depreciation of the new lathe is:
 - Year 1 $3\,000\,000 \times 0.12 = \$360\,000$
 - Year 2 $2\,640\,000 \times 0.12 = \$316\,800$



4. The advantages to Hardy Engineering of using declining balance depreciation might be:

- More accurate reflection of the way assets depreciate
- It allows for changes in technology and asset obsolescence
- Better matching of the cost of an asset with the revenues of an asset when it is new.

The disadvantages are:

- It is based on forecasted residual value and useful life
- It is more difficult to calculate than straight-line depreciation.

Exam practice question

1. Advantages that large supermarket chains might have over Carlos's shop might be:

- Buying food in bulk at lower unit costs
- Brand recognition
- Large-scale capital reduces unit costs.

2. a. Carlos's profit and loss account for 2010:

		\$
Sales	80 000 x 12	960 000
Cost of goods sold	960 000 x 0.75	720 000
Gross profit		240 000
Indirect cost		20 000
Net profits		220 000

b. Annual depreciation expense of the van is: $(\$40\,000 - \$8\,000) / 4 = \$8\,000$

c. The usefulness of Carlos's profit and loss account to different stakeholders might be:

- Banks and other creditors – repayment, risk of default, interest
- Employees – Job security, wages, funds to improve working conditions
- Shareholders – profit and dividends, continued business.



Key concept question

Ethics might be important in producing a set of accounts in terms of fair and accurate view of a business's:

- Profits and asset value for shareholders
- Cash flow and asset value for lenders and creditors
- Cash flow and profits for employees
- Profits for the government
- Profits and asset value for potential investors
- Cash flow and asset value for suppliers
- Profits, cash flow and asset value for the local community.

Without an ethically produced set of accounts, stakeholders may be misled on the business's financial position and may make the wrong decisions because of this.